U. S. Department of Veterans Affairs
FY 1998 Financial Presentation

Financial Contents

CONSOLIDATED BALANCE SHEET
As of September 30, 1998
(dollars in millions)

	Consolidated Total
Assets	
Entity assets	
Intragovernmental:	
Fund balance with Treasury (Note 2)	$13,050
Investments (Note 4)	14,611
Accounts receivable, net (Note 5)	542
Other assets (Note 6)	189
Total intragovernmental	28,392
Investments (Note 4)	$239
Accounts receivable, net (Note 5)	608
Loans receivable and related foreclosed property, net (Note 7)	3,538
Cash and other monetary assets (Note 3)	1
Inventory and related property, net (Note 8)	90
General property, plant and equipment (Note 9)	11,941
Other assets (Note 6)	76
Total entity assets	44,885
Non-entity assets	
Fund balance with Treasury (Note 2)	1,206
Other assets (Note 6)	1
Total non-entity assets	1,207
Total Assets	46,092
Liabilities	
Liabilities covered by budgetary resources	
Intragovernmental:	
Accounts payable	91
Debt (Note 10)	1,777
Other intragovernmental liabilities (Notes 11,12)	2,428
Total intragovernmental liabilities	4,296
Accounts payable	3,384
Liabilities for loan guarantees (Note 7)	4,705
Insurance liabilities (Note 14)	12,935
Other liabilities (Notes 11,12)	2,552
Total liabilities covered by budgetary resources	27,872
Liabilities not covered by budgetary resources	
Federal employee and veteran's benefits payable (Note 13)	579,459
Environmental and disposal liabilities (Note 17)	139
Insurance liabilities (Note 14)	524
Other liabilities (Notes 11,12)	1,262
Total liabilities not covered by budgetary resources	581,384
Total Liabilities	609,256
Net Position	
Unexpended appropriations (Note 15)	4,729
Cumulative results of operations	(567,893)
Total Net Position	(563,164)
Total Liabilities and Net Position	$46,092

The accompanying notes are an integral part of these statements.

CONSOLIDATED STATEMENT OF NET COST

Fiscal Year Ended September 30, 1998

(dollars in millions)

	Consolidated Total
Net Program Costs:	
Medical Care	$17,176
Medical Education	833
Medical Research	575
Compensation	126,267
Pension	3,228
Education	964
Vocational Rehabilitation & Counseling	502
Loan Guaranty	1,378
Insurance	180
Burial	1,314
Net Intra-VA Eliminations	1
Total Net Program Costs	152,418
Costs Assigned to Non-VA Programs	$128
Less: Earned Revenues Attributable to Non-VA Programs	($102)
Net Cost of Operations (Note 19)	$152,444

CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

Fiscal Year Ended September 30, 1998

(dollars in millions)

	Consolidated Total
Net Cost of Operations (Note 19)	$152,444
Financing Sources (other than exchange revenues):	
Appropriations used	42,484
Taxes (and other non-exchange revenue)	3
Donations (non-exchange revenue)	43
Imputed financing	760
Transfers-in	476
Transfers-out	(1,601)
Other financing sources	23
sub-total	42,188
Net results of Operations	(110,256)
Incr/(Decr) in Unexpended appropriations & Non-operating changes	$335
Current Period Change in Net Position	(109,921)
Net Position Reconciliation:	
Net Position, beginning of the period	(453,659)
Prior Period Adjustments: add/(subtract) (Note 22)	416
Current Period Change in Net Position (from above)	(109,921)
Net Position-End of Period	($563,164)

The accompanying notes are an integral part of these statements.

COMBINED STATEMENT OF BUDGETARY RESOURCES (Note 18)
Fiscal Year Ended September 30, 1998
(dollars in millions)

Budgetary Resources	**Combined Total**
Budget authority	$45,109
Unobligated balance- beginning of period	21,007
Net transfers prior-year balance, actual (+ or -)	213
Spending authority from offsetting collections	8,047
Adjustments	(3,248)
Total Budgetary Resources	71,128
Status of Budgetary Resources	
Obligations incurred	51,094
Unobligated balance available	15,107
Unobligated balance not available	4,927
Total Status of Budgetary Resources	71,128
Outlays	
Obligation incurred	51,094
Less: Spending authority from offsetting collections and adjustments	(8,463)
Subtotal	42,631
Obligated balance, net - beginning of period	6,864
Less: Obligated balance, net - end of period	(7,286)
Total Outlays	$42,209

The accompanying notes are an integral part of these statements.

COMBINED STATEMENT OF FINANCING
Fiscal Year Ended September 30, 1998
(dollars in millions)

	Combined Total
Obligations and Nonbudgetary Resources	
Obligations incurred	$51,094
Less: Spending authority from offsetting collections and adjustments	(8,463)
Donations not in the entity's budget	13
Financing imputed for cost subsidies	760
Transfers-in (out)	1,557
Exchange revenue not in the entity's budget	(13)
Nonexchange revenue not in the entity's budget	(1,193)
Other financing sources	(566)
Total obligations as adjusted and nonbudgetary resources	43,189
Resources That Do Not Fund Net Cost of Operations	
Change in amount of goods, services, and benefits ordered but not yet received or provided (net increase)/net decrease	257
Change in unfilled customer orders	77
Costs capitalized on the balance sheet (increases)/decreases	(4,613)
Financing sources that fund costs of prior periods	(216)
Other	2,152
Total resources that do not fund net costs of operations	(2,343)
Costs That Do Not Require Resources	
Depreciation and amortization	858
Bad debts related to uncollectible non-credit reform receivables	183
Revaluation of assets and liabilities	(24)
Loss on disposition of assets	236
Other	0
Total costs that do not require resources	1,253
Financing Sources Yet To Be Provided	110,345
Net Cost of Operations	$152,444

The accompanying notes are an integral part of these statements.

Notes to the Financial Statements

Tabular dollars in millions

NOTE 1 Summary of Significant Accounting Policies

Reporting Entity

Created by Congress (1930) as the Veterans' Bureau, it was renamed the Veterans Administration, then was accorded Cabinet rank on March 15, 1989 to become the Department of Veterans Affairs. By law, "the purpose of the Department is to administer the laws providing benefits and other services to veterans and the dependents and the beneficiaries of veterans (38 U.S.C.}301(b), 1997)."

In recognizing their service to the Nation, VA serves America's veterans and their families with profound respect and compassion; is their principal advocate in promoting the health, welfare, and dignity of all veterans; and ensures that they receive medical care, benefits, social support and lasting memorials.

Basis of Accounting

The VA accounted for its appropriations and funds in four lines of business: Veterans Health Administration, Veterans Benefits Administration, National Cemetery Administration, and Departmental Administration. The financial statements have been prepared in accordance with Form and Content guidance specified by the Office of Management and Budget (OMB) and the Statements of Federal Financial Accounting Standards (SFFAS).

Investments in U.S. Government Securities

Investments in U.S. Government Securities are reported at cost and are redeemable at any time for their original purchase price.

Public Accounts Receivable

Although VA actively participates in Federal Debt Collection programs like the IRS Income Tax Refund Offset, Federal Salary Offset, Litigation, Referral to Credit Reporting Agencies, and Referral to Private Collection Agencies, there are still a number of accounts which will successfully circumvent all available collection efforts. For these, an allowance for uncollectible accounts is established.

Property and Equipment

The majority of the reported property represents facilities and equipment used to provide medical care to veterans. Property and equipment, including transfers from other Federal agencies, are valued at cost. Expenditures for major additions, replacements, and alterations are capitalized. Routine maintenance is expensed when incurred.

Construction costs are capitalized as Construction in Progress until completion, then transferred to the appropriate property account. Individual items are capitalized if the unit price is $5,000 or greater and useful life is two years or more. Buildings are depreciated straight-line over estimated useful lives of 25 to 40 years. Equipment is also depreciated straight-line over its useful life, usually 5 to 20 years

All VA heritage assets are multi-use facilities and are classified as general property, plant and equipment.

Accrued Compensation and Pension Benefits

Compensation and pension benefits are accrued when veterans have satisfied VA's eligibility criteria. This accrual pertains only to benefits due and payable in a particular fiscal year.

Life Insurance Program Liabilities

VA life insurance programs receive the majority of the funding needed to support the programs from premiums paid by policyholders and interest earned on U.S. Government securities. Appropriated funds are required to meet the operating deficits of the Service Disabled Veterans Insurance (SDVI) and Veterans Insurance and

Indemnity (VI&I) programs. Appropriations are recognized as revenues at the time that they are received to fund the operating deficits and claims.

Other revenues are recognized when earned.

The Service Disabled Veterans Insurance Fund is augmented by budget appropriations.

Policy reserve liabilities are based on mortality tables and interest assumptions prescribed by Federal statutes and are designed to be sufficient to provide for guaranteed policy benefits.

These policy reserve liabilities, as well as liabilities for disability waiver of premium benefits and incurred death and disability installment claims, are included in Insurance Liabilities.

Liabilities for unpaid claims in process of settlement and experience-based estimates of claims incurred but not reported are classified as Accounts Payable. Liabilities for the SDVI and VI&I programs for which an appropriation has not been enacted are classified as Insurance Liabilities Not Covered by Budgetary Resources.

Future Liability for Veterans Compensation and Burial Benefits

These unfunded liabilities represent the future liability for veterans' disability compensation and burial benefits as required by SFFAS No. 5, which requires recognition of an actuarial liability for veterans' benefits.

Insurance Interest Payable

Insurance interest payable is interest earned on dividends left on deposit and paid annually to insurance policyholders on their policy anniversary dates.

Unfunded Expenses

Unfunded expenses include accrued program expenses customarily financed by appropriations. The cumulative amount for which appropriations have not been enacted is classified as an unfunded liability.

Losses on Guaranteed Loans

Upon foreclosure of a guaranteed loan, VA may be required to pay the maximum claim, acquire the property, or acquire the property and pay less than the maximum claim pursuant to criteria established in 38 U.S.C.§ 3732. Thus, when VA acquires the property, the ultimate program cost is comprised of the claimed amount paid the lender less net proceeds from the sale of the property. VA incurs an additional cost for direct home (vendee) loans, issued upon the sale of foreclosed properties that subsequently default.

Loans made after September 30, 1991 are subject to the provisions of the Credit Reform Act of 1990. The liability provision for future losses on credit reform guaranteed loans is comprised of a funded subsidy for each loan guaranteed at the rate equal to the amount of the present value of estimated loss to the government for the cohort of loans. The subsidy amounts for each cohort are reestimated annually to ensure that the amounts are reflective of the actual losses on guaranteed loans. Based on the reestimated amounts, additional subsidy funds are provided or excess funds are returned.

Loans made prior to October 1, 1991, remain subject to the procedures and accounting methods in effect preceding credit reform. Estimated losses on anticipated defaults of pre-credit reform guaranteed loans are recorded as expenses when the loans are guaranteed (as loan loss reserves). A liability provision is simultaneously established representing the estimated cost of defaults for those guaranteed loans indicating probable future default. A portion of this provision is subsequently reclassified as a reduction to: (1) direct home loans receivable when such loans are issued (see Note 7); (2) foreclosed property held for sale when property is acquired, recording such property at its net realizable value and; (3) investments in subordinate securities reflecting the estimated loss of principal for the securities due to their subservient position. The remainder of the provision for loan losses is classified as a liability for future loan losses.

Revenues and Financing Sources

The United States Constitution prescribes that funds must be made available by congressional appropriation before they may be expended by a federal agency. Most of the Department's operating funds originates from congressional appropriations. Additional funds are obtained through reimbursements for services performed for other federal agencies and the public.

Recognition of Financing Sources

Exchange revenues are recognized when earned. Expenses generally are recognized when incurred and non-exchange revenues are recognized on a modified cash basis. Remittances of non-exchange revenues are recognized when received and related receivables are recognized when measurably and legally collectible, as are refunds and related offsets. This basis of accounting differs from that used for budgetary reporting. All significant intra-agency balances and transactions have been eliminated in consolidation.

Interest income, which is earned primarily from the investments of VA's life insurance program, is recognized on the accrual basis. Insurance premiums are recognized as revenue when due. Loan origination fees are recognized as revenues at the time of the guaranty.

The current congressional budgetary process under which VA operates does not distinguish between capital and operating expenditures. For these purposes, both are recognized as a use of budgetary resources (outlays) as paid. For financial reporting purposes under accrual accounting, operating expenses are recognized currently, while those for capital and other long-term assets are capitalized and not recognized as expenses until actually used. Financing sources for these expenses, which are derived from both current and prior year appropriations and operations, are also recognized this way.

For certain accrued expenses (e.g., annual leave earned but not taken, future period veterans compensation and burial benefits, and insurance premiums for disabled veterans funded by appropriations), current or prior year appropriations aren't available to fund them. These expenses are usually financed (funds appropriated) in the year payment is made. Amounts due from future financing sources is therefore recognized in operations each year for that year's accrued expenses. These cumulative accruals are disclosed in the Consolidated Balance Sheet as a reduction of total net position. The statements represent a U.S. Government Department - a sovereign Entity. The unfunded liabilities reported in them, dependent on federal financing, can't be liquidated without enacting an appropriation law. Statement users must realize that payment of liabilities other than contracts can be abrogated by the Sovereign Entity.

Annual, Sick, and Other Types of Leave

Annual leave is accrued when earned and the accrual is reduced when leave is used. At least once a year, the balance in the accrued annual leave account is adjusted to reflect current pay rates of cumulative annual leave earned but not taken. Sick and other types of leave are expensed as taken.

Trust Fund Balances

Trust fund balances consist of the Post-Vietnam Educational Assistance Trust Fund, National Service Life Insurance (NSLI) Fund, United States Government Life Insurance (USGLI) Fund, Veterans Special Life Insurance (VSLI) Fund, General Post Fund, National Cemetery Gift Fund, Transitional Housing Loan Program Account and the Transitional Housing Loan Financing Account. These funds are accounted for separately and their use is restricted.

Workers Compensation

Legal actions brought by VA employees for on-the-job injuries fall under the Federal Employees Compensation Act (FECA) administered by the Department of Labor (DOL). DOL bills each agency annually as its claims are paid; however, payment on these bills is deferred two years to allow for funding through the budget process. Using actuarial estimates provided by DOL, VA recorded FECA liabilities for balances billed to VA and for estimates of the present value of the long-term payments related to cases on hand at the end of the fiscal year.

Imputed Financing

Imputed Financing is recorded on VA's financial statements when another federal entity pays for expenses that are attributable to VA operations.

Imputed financing is recorded for settlement payments on legal cases made by the Treasury Judgment Fund on VA's behalf and retirement benefits paid by OPM for VA employees.

NOTE 2 Fund Balances with Treasury

The U. S. Department of Treasury performs cash management activities for all government agencies. The fund balance with Treasury represents the right of the Department to draw on the U. S. Treasury for allowable expenditures.

Fund Balances with Treasury Funding Year 1998

Entity Assets	VHA	VBA	NCA	ADM	Totals
Trust Funds	$ 3	$ 134	$ -	$ -	$ 137
Revolving Funds	62	4,629	-	134	4,825
Appropriated Funds	5,698	2,133	36	162	8,028
Special Funds	55	-		-	55
Other Fund Types	-		-	6	6
Entity Totals	$5,817	$6,896	$36	$301	$13,050
Non-Entity Assets					
Special Funds	-	$1,152	-	$ -	$1,152
Other Fund Types			-	54	54
Non-Entity Totals	$ -	$1,152	-	$54	$1,206
Reconciliation of VA General Ledger Balances with Treasury					
Fund Balance with Treasury	$5,817	$6,896	$36	$301	$13,050
Reconciled Differences	21	1		(1)	21
Unreconciled differences	-	11	-	-	11
Entity VA General Ledger	$5,838	$6,908	$36	$300	$13,082

NOTE 3 Cash, Foreign Currency, and Other Monetary Assets

The VA Canteen Service is the only VA fund which deposits cash in commercial banks for future use. The Canteen Service held $0.8 million in commercial bank accounts at the end of fiscal year 1998.

Cash advanced to imprest fund cashiers totaled $5.1 million at September 30, 1998.

All other cash receipts and disbursements are processed by the Department of the Treasury.

NOTE 4 Investments

Insurance program investments, which comprise most of VA's investments, are in non-marketable U.S. Treasury special bonds and certificates. Interest rates for Treasury special securities are based on average market yields for Treasury issues. The special bonds, which mature during various years through the year 2013, are generally held to maturity unless needed to finance insurance claims and dividends. Other VA programs investments are in securities issued by the Department of the Treasury with the exception of the Housing Credit Assistance Program investments which are in trust certificates that were issued by the American Housing Trust, a private entity not associated in any way with the Government.

Investment Securities as of September 30, 1998

Intragovernmental Securities:	Interest Range	VHA	VBA	Total
Special Bonds	5.87-13.75%		$ 14,243	$ 14,243
Treasury Notes *	5.11-9.125%	$ 45		45
Treasury Bills	4.74-5.29%	38		38
Subtotal		83	14,243	14,326
Accrued Interest		1	284	285
Total		$ 84	$ 14,527	$ 14,611
Other Securities:				
Trust Certificates (Housing Credit) **			$ 239	$ 239

*The investment in Treasury notes includes unamortized premiums of $.3 million as of September 30, 1998. Premiums and discounts are amortized on a straight-line basis over the life of the investments.

**The trust investments constitute the only investments in certificates not issued by the Department of the U. S. Treasury.

NOTE 5 Accounts Receivable

VHA public accounts receivable mainly consist of amounts due from patients and third-party insurers for veterans healthcare. These funds are collected through the Medical Care Collections Fund (MCCF). MCCF receivables totaled $878 million at September 30, 1998. These MCCF receivables were offset by an Allowance for Contractual Adjustments of $421 million to recognize differences between revenue at established rates and amounts realizable from third-party payers under contractual agreements.

VBA public accounts receivable are primarily composed of amounts due from individuals for compensation, pension, and readjustment benefit overpayments.

Based on prior experience, allowance for bad debt losses have been established at approximately 18% for MCCF receivables and at 75% for benefit overpayments.

Federal accounts receivable are mostly upward subsidy reestimates due from the Treasury Department.

Accounts Receivable as of September 30, 1998

	VHA	VBA	ADM	Total
Intragovernmental Accounts Receivable	$ 41	$459	$42	$542
Public Accounts Receivable Gross	910	664	12	1,586
Allowance for Contractual Adjustments	(421)	-	-	(421)
Allowance for bad Debts	(89)	(468)	-	(557)
Net Public Accounts Receivable	$400	$196	$12	$608

NOTE 6 Other Assets

VHA non-federal advances include advance payments to: hospitals and medical schools under house staff contracts, grantees, beneficiaries, and employees on official travel. VBA non-federal advances include $37.9 million on deposit with trustees for offset against loan loss claims related to sold portfolio loans. Federal advances are primarily to GSA for supplies and equipment.

Other Assets as of September 30, 1998

	VHA	VBA	ADM	Total
Other Entity Assets				
Intergovernmental advance payments	$86	$ -	$103	$189
Public advance payments	32	43	1	76
Other non-entity assets intragovernmental	-	-	1	1
Total	$118	$43	$105	$266

NOTE 7 Loans Receivable, Non-Federal Borrowers

Vocational Rehabilitation Revolving Fund

The Federal Credit Reform Act of 1990 included the Vocational Rehabilitation Revolving Fund in credit reform. This fund provides cash advances based on entitled future benefits (non interest bearing loans) to veterans for purchasing educational equipment and supplies while attending an approved training program. The advances are recovered through benefit deductions over a period of four to six months. As of the end of FY 1998, $2.2 million had been advanced and $1.4 million or 63% had been collected. The number of loans issued were 4,324, an average of $489, for each loan. This fund has historically been financially sound because most of the advances are recovered directly from C&P benefits.

Education Loan Fund

The Education Loan fund has also been placed under credit reform. The main function of this fund is to record collections of loans issued prior to credit reform. The Education Loan fund disbursed loans to veterans attending an approved educational program. There have been no loans disbursed since FY 90.

Insurance Program

Policyholders in the life insurance programs with permanent plan coverage may borrow up to 94 percent of the cash value of their policies. In the past, all policy loans carried fixed interest rates. However, policy loans issued after November 2, 1987, have a variable interest rate with a minimum of 5% and a maximum of 12%, depending on U.S. Treasury security rates. The interest rate during fiscal years 1998 and 1997 was 6%.

Policy loans do not have a fixed repayment schedule as long as the policy loan does not exceed the reserve value of the policy. The policyholder may repay the loan at their discretion. On an annual basis, any unpaid interest becomes part of the loan principal and bears interest in the same manner. Loans are accounted for as receivables after funds have been disbursed. Policyholder loans are not subject to the Federal Credit Reform Act.

Housing Credit Assistance Program

Activities under VA's Housing Credit Assistance Program primarily involve the partial guaranty of residential mortgage loans issued to eligible veterans by private lenders. In addition, VA originates direct loans to veterans, sells foreclosed property on credit terms (vendee loans) to veterans and non-veterans, and monitors foreclosure settlements for ultimate claims reimbursement to VA.

Residential loans guaranteed by VA are originated by private lenders and are not recorded in the financial statements of VA. However, VA does record a liability for a partial guaranty of these loans. In FY 1998, the following is VA's outstanding guaranteed loans:

Outstanding Principal, Guaranteed Loans Face Value	Amount Outstanding Principal Guaranteed
$203,451	$70,032

As of September 30, 1998, VA held 12,542 foreclosed properties. The estimated average holding period for these properties was 6.2 months. Also, there were 16,396 properties for which foreclosure proceedings were in process as of September 30, 1998.

Vendee, Refunded and Direct Loans

The total amount of these loans established during Fiscal Year 1998 are:

Vendee loans	$1,206
Refunded loans	133
Direct loans	3
Total	$1,342

Loans Receivable

Loans receivable primarily represents the net value of assets related to pre-1992 and post-1991 direct loans and acquired defaulted guaranteed loans related to the Housing Credit Assistance Program. Those assets are comprised of loans receivable, interest receivable and related foreclosed property. They are offset by an allowance for estimated uncollectible loans and interest or an allowance for subsidy cost. The components of loans receivable are as follow as of September 30, 1998:

Direct Loans	
Pre-1992 (Allowance for Loss Method)	
Loans Receivable,Gross	$ 297
Interest Receivable	36
Allowance for Loan Losses	(76)
Foreclosed Property	118
Value of Assets Related to Direct Loans	$375
Post-1991 (Present Value Method)	
Loans Receivable, Gross	$ 1,162*
Interest Receivable	12
Foreclosed Property	14
Allowance for Subsidy Cost (PV)	(299)
Value of Assets Related to Direct Loans	889
Total Direct Loans,Net	$1,264

*Includes $.8 million in direct loans for the vocational rehabilitation program.

Guaranteed Loans	
Pre-1992 (Allowance for Loss Method)	
Defaulted Guaranteed Loans Receivable, Gross	$ 614
Allowance for Loan Losses	(589)
Foreclosed Property	129
Defaulted Guaranteed Loans Receivable, Net	$154
Post-1991 (Present Value Method)	
Defaulted Guaranteed Loans Receivable, Gross	$ 156
Foreclosed Property	998
Value of Assets Related to Defaulted Guaranteed Loans Receivable	1,154
Total Guaranteed Loans, Net	$1,308
Insurance Policy Loans	
Loans Receivable, Gross	$ 941
Interest Receivable	25
Total Insurance Policy Loans	$966
Total Loans Receivable and Related Foreclosed Property, Net	$3,538

Liability for Loan Guarantee Programs

The liability for FY 98 loan guarantees represents the present value of the estimated net cash flows to be paid by VA as a result of the guarantee. The following is the liability for the post-1991 loan guarantees:

Liabilities for loan guarantees for Post-1991 guarantees present value	
Housing credit	$4,705.

Subsidy Expense

Pursuant to the Credit Reform Act, all direct loans established and guaranteed loans closed after September 30, 1991, will be subsidized. The subsidy expense for direct loans and loan guarantees primarily related to the Housing Credit Assistance Program is as follows:

Subsidy Expense for Direct Loans and Loan Guarantees

	Direct Loans	Guranteed	Total
Interest Difference and Supplemental	$(760)	$	$ (760)
Defaults	553*	2,331	2,884
Fees	(298)	(1,712)	(2,010)
Other	986	(180)	806
Reestimates	6	159	165
Total subsidy expenses	$ 487	$ 598	$1,085

Provision for Losses on Pre-1992 Loans

One element of the cost of the mortgage loan benefit that VA provides to veterans is the present value of the cost VA will bear as loans already guaranteed default in the future. This cost is reflected in the financial statements as an offset to the value of certain related assets.

The provision for losses on guaranteed loans is based upon historical loan foreclosure results applied to the average loss on defaulted loans. The provision calculation is also based on the use of the average interest rate of the U.S. interest-bearing debt as a discount rate on the assumption that VA's outstanding guaranteed loans will default over a twelve-year period. The discount rate used in the calculation was 6.7 percent for FY 1998. The components of the provision are as follows as of September 30, 1998:

Offsets against loans receivable	$ 36
Offsets against foreclosed property held for sale	23
Offset against investments	46
Reserve for Losses on Guaranteed Loans	40
Total	$145

Loan Sales

The Department of Veterans Affairs continues to have vendee loan sales to meet the budget commitments of the Loan Guaranty Program. During the period FY 1992 through FY 1997, the total loans sold amounted to $7.8 billion. VA completed three sales during fiscal year 1998 totaling approximately $1.1 billion of vendee loans to Vendee Mortgage Trust. The components of the vendee sales are summarized in the table below:

Loans receivable sold	$1,129
Proceeds from sale*	1,170
Loss (Gain) on receivables sold	$ (41)

*Information presented does not reflect the transaction expenses incurred to sell the loans.

All loan sales after September 30, 1991 are subject to Credit Reform requirements. These sales contain two types of guarantees. The VA guarantees that the principal and interest payment due on a loan sold will be paid by the 15th of each month. If not paid by the borrower, VA allows the loan servicer to take funds from cash reserve accounts for the deficient amount. The VA also guarantees the loans against losses at foreclosure. VA will not buy back the loans but will pay off loan losses and foreclosure expenses.

Offset For Losses on Investments

As of September 30, 1998, an allowance was recorded to reflect an estimated loss of principal as a result of the subordinated position in American Housing Trust I-V certificates. The estimated allowance computation was based upon historical loan defaults. The net investment balances are as follows:

American Housing Trust I-V

Investment in subordinated certificates of securities at time of sale	$424
Cumulative reductions	(139)
Subtotal	285
Allocation of loss provision	(46)
Net Investment	$239

These subordinated certificates have been pledged as collateral to support recourse loans made under American Housing Trust VI through XI and the "Vinnie Mac" program. Although the VA no longer has legal title to these subordinated securities, the Department has a contingent interest in any residual income that these certificates earn. The income earned on these certificates covers the amount of the realized losses for American Housing Trust VI through XI and the "Vinnie Mac" program and any residual income reverts to VA.

Contingent Liability

As the VA continues to sell vendee loans, the Department has an increasingly large potential liability related to sales amounts which it has guaranteed. This liability is related to VA's full guaranty of the principal and interest payments on sold loans. VA's actual liability is expected to be much less than the sales amount. Historically, the loss rate on portfolio loans has been about 3-4 percent.

Guarantee Commitments

As of September 30, 1998, VA had outstanding commitments to guarantee loans which will originate in FY 1999. The number of commitments could not be determined, as VA has granted authority to various lenders to originate VA loans that meet established criteria without prior VA approval. Nearly 90 percent of VA's guaranteed loans originate under this authority.

Note 8 Inventory and Related Property Inventories

VA inventories are valued at the lower of cost or market. Merchandise inventory includes burial flags, general supplies, precious metals held for sale, and Canteen retail store stock. There are no changes in prior year's accounting methods.

VA Inventories	VHA	ADM	FY 1998
Inventory held for current sale	$34	$38	$72
Excess, obsolete and unservicable inventory	17		17
Inventory held for repair and parts		1	1
Total	$51	$39	$90

Operating Materials & Supplies

Operating materials and supplies mostly consist of Medical Supplies, pharmaceuticals and general office supplies that are in the hands of the end user for normal operations. Since it is not cost beneficial to the VA to apply the consumption method of accounting, VA adopted the Purchases Method, which provides that operating material and supplies be expensed when purchased. There are no changes in prior year's accounting methods.

Stockpile Materials, Seized Property, and Forfeited Property

The VA maintains no stockpile materials, seized or forfeited property. See Note 7 for discussion on VA's accounting for foreclosed properties.

Goods Held Under Price Support and Stabilization Programs

The VA does not maintain goods held under price support and stabilization programs.

NOTE 9 Property and Equipment

Major classes of general property, plant and equipment, method(s) of depreciation, capitalization thresholds, and restrictions on the use or convertibility of general PP&E are discussed in Note 1 of the Financial Statements. Current year depreciation totaled $858 million in FY 1998. The following table provides property and equipment data as of September 30, 1998.

	Cost	Accumulated Depreciation	Net Book Value
Land and improvements	$ 166	$ -	$ 166
Buildings	12,805	4,945	7,860
Equipment	4,654	2,511	2,143
Other	1,572	837	735
Construction in progress	1,037	-	1,037
Total	$20,234	$8,293	$11,941

NOTE 10 Debt

Intragovernmental debt:	
VBA	$1,776
Administration	1
Total	$1,777

All intragovernmental debt is due to the U.S. Treasury and is related to borrowing by the Housing Credit Program. VA's financial activities interact with and are dependent upon those of the Federal Government as a whole. Thus, VA's financial statements do not reflect the results of all financial decisions and activities applicable to VA as if VA were a stand-alone entity.

VA's consolidated financial statements are not intended to report the Department's proportionate share of the Federal deficit or public borrowing including interest thereon. Financing for budget appropriations reported on the financial statements could be derived from tax revenues or public borrowing, or both; the ultimate source of this financing, whether it be tax revenues or public borrowing, has not been specifically allocated to VA. Financing for major and minor construction projects was obtained through budget appropriations. To the extent that this financing was derived from public borrowing, no interest has been capitalized because such borrowings are recorded in total by the Department of the Treasury and are not allocated to individual Departments and agencies.

VA does not have the authority to issue debt instruments to any government agency or the public.

NOTE 11 Other Liabilities

Other Liabilities Covered by Budgetary Resources:

	VHA	VBA	NCA	ADM	Total
Intragovernmental					
Deposit & Clearing Acct Liability	$ -	$ -	$ -	$ 10	$ 10
Deferred Revenue	-	6	-	8	14
Resources Payable to Treasury	-	809	-	-	809
Subsidy Reestimates	-	1,587	-	-	1,587
GFR Liability	-	-	-	8	8
Total	**$ -**	**$2,402**	**$ -**	**$ 26**	**$2,428**
Public					
Deferred Revenues	$ -	$ -	$ -	$ -	$ -
Accrued Salaries and Benefits	533	-	3	48	584
Unredeemed Coupons	1	-	-		1
Deposit & Clearing Acct Liability	-	-	-	48	48
Unearned Premiums	-	150	-	-	150
Insurance Dividends left on Deposit		1,390	-	-	1,390
Capital Lease Liability	24	-	-	-	24
Judgement Fund - Funded	2	-	-	-	2
Dividend Payable to Policyholders	-	351	-	-	351
Custodial Liability	-	2	-	-	2
Total	**$ 560**	**$1,893**	**$ 3**	**$ 96**	**$2,552**

Other Liabilities not Covered by Budgetary Resources:

	VHA	VBA	NCA	ADM	Total
Public					
Annual Leave	$ 823	$ -	$ 4	$ 55	$ 882
Capital Lease Liability	1	-	-	2	3
Judgement Fund - Unfunded	67	-	-	-	67
Accrued FECA Liability	296	-	4	10	310
Total	**$1,187**	**$ -**	**$ 8**	**$ 67**	**$1,262**

NOTE 12 Leases

Entity as Leases
Capital Leases

Summary of Assets Under capital Lease:

Present Value:	Land and Buildings	$ 28
	Less Accumulated Amortization	1
	Net Book Value	$ 27

VHA utilizes these Capital Leases to acquire space for Outpatient Clinics.

Future Payments Due by Capital Lease

	Albuquerque, NM	Charleston,SC	Columbus, OH	Redding, PA	Totals
1999	$1	$0	$1	$1	$ 3
2000	$1	$0	$1	$1	$ 3
2001	$1	$0	$1	$1	$ 3
2002	$1	$0	$1	$1	$ 3
2003	$1	$0	$1	$1	$ 3
After 2003	$5	$5	$14	$4	$ 27
Total Future Lease Payments	$9	$6	$21	$7	$ 42
Less: Imputed Interest	$2	$2	$6	$2	$ 13
Executory Costs	$1	$1	$2	$1	$ 5
Net Capital Lease Liability	$5	$3	$12	$4	$ 24

Liabilities covered by budgetary resources	$ 24
Liabilities not covered by budgetary resources	$ 1

Note: Totals do not add due to rounding.

NOTE 13 Federal Employee and Veterans Benefits

Unfunded Federal Employee and Veterans Benefits liability as of September 30, 1998:

Federal Employee Compensation Act (FECA) actuarial liability	$ 1,310
Disability compensation and burial liability	578,149
Total	$579,459

A summary of how these amounts were determined follows.

FECA Liability

VA used actuarial estimates provided by the Department of Labor (DOL) based in part on past claims arising from VA employees when recording an unfunded liability for future workers compensation claims. However, once claims are actually billed to VA they are recorded as an "Other liability" on the balance sheet (see note 11).

Overview of Veterans Benefits

Veterans or their dependents receive disability compensation benefits if the veteran was disabled or died from military service-connected causes. War veterans or their dependents receive pension benefits based on annual eligibility reviews, if the veteran was disabled or died from non service-connected causes. Certain pension benefits are subject to specific income limitations. Veterans and service members who die on active duty and their dependents are eligible for burial in one of VA's 115 national cemeteries. Additionally, the NCA provides a burial and plot allowance for burial in private cemeteries, burial flags, headstones and markers and graveliners to the family of eligible service persons. These benefits are not subject to income limitations and are provided in exchange for a veteran's military service.

VA has a liability for benefits expected to be paid in future fiscal years to veterans and, if applicable, their survivors who have met or are expected to meet defined eligibility criteria. The future liability of the disability compensation, pension and burial programs (C&P) is not currently funded, nor is there any intent to do so. Payments for benefits that become due in a particular year are financed from that year's appropriation, on a pay-as-you-go basis. Payments of the future liability rely on congressional authorization of future tax revenues or other methods, such as public borrowing for their financing.

Disability Compensation and Burial Actuarial Liability

The future liability for disability compensation and burial benefits is recorded as an unfunded liability on the balance sheet in accordance with SFFAS No. 5. The change in the actuarial present value of the future liability for disability compensation and burial benefits from September 30, 1997 to September 30, 1998 is as follows:

	FY 1997	Increase	FY 1998
Compensation	$465,715	$108,712	$574,427
Burial	2,638	1,084	3,722
Total	$468,353	$109,796	$578,149

The net increase in the actuarial present value of the future liability for disability compensation and burial benefits from 1997 to 1998 is recognized in the Statement of Net Cost.

Pension Benefits Actuarial Liability

The actuarial present value of the future liability for pension benefits is disclosed herein but not recorded on the balance sheet in accordance with SFFAS No. 5. The pension program is a needs based program in which the beneficiaries are subject to income limitation eligibility screening. Many pension payments are made to survivors of deceased veterans. Accordingly, it has been determined that the pension program payments are non-exchange transactions or non-reciprocal payments since the payments are not based on services received. The accounting for this liability is similar to accounting for social insurance programs (e.g. Food Stamps.)

The change in the projected liability for pension benefits as determined by VA at September 30, 1997 and September 30, 1998 is as follows:

	FY 1997	Increase	FY 1998
Pensions	$73,414	28,413	$101,827

Actuarial Assumptions

The significant actuarial assumptions used in the September 30, 1998 valuation of disability compensation, pension and burial benefits were:

A. To calculate the present value of the liability, future cash flows were discounted in perpetuity. A liability was recognized for the projected benefit payments to: (1) those beneficiaries, including veterans and survivors, currently receiving benefit payments, and (2) current veterans who will in the future become beneficiaries of the C&P programs, and (3) a proportional share of those in active military service as of the valuation date who will become veterans in the future. The proportional share representing the percentage of total active service accrued through the valuation date. Survivors of those veterans in classes (1), (2) and (3) who receive benefits after the death of the veterans are also incorporated into the projection.

B. Discount rates were based on rates on securities issued by the Treasury on September 30, 1998, ranging from 4.41% to 4.98%, and on September 30, 1997, ranging from 5.47% to 6.47%. Cash flows were assumed to occur at the midpoint of the fiscal year.

C. All calculations were done by program. The calculation for pension benefits was performed separately for each law: Old Law, Sec. 306, and P.L. 95-588. Burial liabilities were calculated on an overall basis.

D. Dollars by category, and by age, were used in the liability for C&P benefits. Therefore, ratios, trends in caseloads, and mortality tables, were used to allocate dollars in these areas.

E. Life expectancy of veterans is based upon studies by VA actuaries in relation to the Service Disabled Veterans Insurance (SDVI) Fund adjusted to 1991 and supplemented by adjusted 1991 U.S. Life mortality for males in early years. The life expectancies for elderly males were determined using the 1994 Uninsured Pensioners mortality table. These rates were brought forward to the present by applying mortality improvements at a rate of 1% per annum. The SDVI study contains mortality information for ages 41 through 75 inclusive.

F. Cost of living adjustments (COLAs) were applied to determine the average benefits per veteran, for each future time period. COLAs of 2.8% and 3.1% were assumed for fiscal years 1997 and 1998, respectively. For fiscal years after 1998, COLAs were determined from the Congressional Budget Office's inflation rate projection and range from 2.5% to 3.1% over the 30-year period. COLAs were applied to all disability compensation benefits and only to P.L. 95-588 pension benefits. (COLA of 1.3% as of 12/1/98 was used for this calculation).

G. Expected benefit payments have been explicitly modeled for the next seventy-one years. This period is roughly the same as that used by the Office of the Actuary of the Social Security Administration (seventy-five years).

H. A public law went into effect on October 1, 1998 permitting surviving spouses whose Dependency and Indemnity Compensation (DIC) benefits had previously been terminated as a result of remarriage, and have subsequently become divorced or widowed, to begin collecting DIC benefits again. An estimate of such benefits was incorporated into the model by increasing the rate of new disability compensation cases by five percent beginning in fiscal year 1999. The effect of this change is to increase the present value of future benefits by about $3.2 billion.

Changes were made to the actuarial assumptions used in determining the estimate of future disability compensation, pension and burial claims from the prior year. Specifically, estimates were made to consider future claims pertaining to active military persons who are not yet considered veterans but will be upon discharge from service, and their future survivors. This change had the effect of increasing the total combined (including pension) liability as of the September 30, 1998 by about $15 billion. However the most significant factor increasing the liability over last year's estimate was decreasing interest rates. The interest rate as of September 30, 1998 was the lowest rate for the most recent three years. The lower interest rates increased the present value of the projected liability by about $85 billion. Other differences in assumptions made, and changes in the beneficiary population resulted in an increase of about $38 billion. A portion of this may be attributable to a downward trend in the rate of new beneficiaries of veteran pension claims during the experience period used. The average rates for the four year experience period were selected for the base case assumptions, rather than selecting the rates from the last few years or a trend in these rates.

Employee Retirement Systems and Benefits

During FY 1998, about 83,000 VA employees continued to participate in the contributory Civil Service Retirement System (CSRS), which was closed to new employees on January 1, 1987. VA makes contributions to the CSRS pension trust fund [which is maintained by the U.S. Office of Personnel Management (OPM)] on behalf of VA employees covered by the CSRS retirement system. However, VA is not required to fully fund the CSRS pension liability pertaining to VA employees because OPM subsidizes the CSRS pension cost. However, VA is required to recognize an expense and impute a financing source for the estimated total cost of the pension benefits pertaining to current employees. Additionally, VA does not fund other post-retirement benefits such as the Federal Employees Health Benefit (FEHB) Program and the Federal Employees Group Life Insurance (FEGLI) Program, but is required to recognize an expense and impute a financing source for the estimated total cost which is fully financed by OPM. The total expense that VA recognized for current employee's retirement benefits described above was $694 million for FY 1998 as shown:

Recognized Expense	**FY1998**
CSRS	$273
FEHB	420
FEGLI	1
Total	$694

On January 1, 1987, the new Federal Employees Retirement System (FERS) went into effect pursuant to Public Law 99-335. During FY 1998 approximately 155,000 VA employees participated in FERS. Employees participating in FERS are covered under the Federal Insurance Contributions Act (FICA), to which VA contributes an amount matching employee withholdings to the Social Security Administration. VA has no liability for future payments to employees under these programs, but the Federal Government is liable for future payments to employees through the various agencies administering the programs.

VA's total contributions for both CSRS and FERS participants, including contributions to the Social Security Administration, during FY 1998 are shown:

VA's Total CSRS, FERS and FICA Contributions

CSRS	$ 292
FERS	747
FICA	466
Total	$1,505

The difference between the amount of expense reported and the contributions made by VA is considered imputed financing on the financial statements.

Note 14 Insurance Programs

VA directly administers six life insurance programs for veterans:

1. United States Government Life Insurance, established in 1919 to handle new issues and the conversion of World War I War Risk Term Insurance;

2. National Service Life Insurance, established in 1940 to meet the needs of World War II service personnel;

3. Veterans Special Life Insurance, established in 1951 for Korean veterans who did not have service-connected disabilities;

4. Service-Disabled Veterans Insurance, established in 1951 for veterans with service-connected disabilities;

5. Veterans Reopened Insurance, a one-year reopening in 1965 of National Service Life Insurance for certain disabled World War II and Korean veterans;

6. Veterans Mortgage Life Insurance, established in 1971 to provide insurance to veterans who have received Specially-Adapted Housing grants.

VA also supervises the administration of the Servicemembers' Group Life Insurance (SGLI) program and a subprogram of SGLI, the Veterans' Group Life Insurance (VGLI) program. SGLI is directly administered by the Prudential Insurance Company of America. This coverage is provided to active members of the Military Services, cadets attending service academies, and active members of the Armed Forces Reserves, National Guard and Reserve Officers Training Corp.

Veterans Life Insurance Activities

The accompanying financial statements reflect the financial decisions and activities directly related to the Life Insurance programs of the Veterans Benefits Administration, Department of Veterans Affairs. Day-to-day operations of the programs are impacted by both VA and other Federal agencies. Specifically, the SDVI, VI&I and Veterans Mortgage Life Insurance (VMLI) programs receive appropriations to meet their operating deficits. The National Service Life Insurance (NSLI) and United States Government Life Insurance (USGLI) programs receive appropriations to fund claims traceable to the extra hazards of military service. The NSLI, USGLI, SDVI, Veterans Special Life Insurance (VSLI) and Veterans Reopened Insurance (VRI) programs receive appropriations to fund the cost of overpayments waived.

The Servicemembers' Group Life Insurance (SGLI) and Veterans' Group Life Insurance (VGLI) programs are administered by VA through a group policy with the Prudential Life Insurance Company of America. Premiums are set by mutual agreement of VA and Prudential. SGLI premiums for Active Duty service personnel, ready Reservists, and Reservists with part-time coverage are deducted from their pay and remitted by each uniformed service to VA, which in turn remits them to Prudential. Veterans insured under VGLI send their premiums directly to Prudential.

VA also monitors Prudential reserve balances to determine their adequacy and may increase or decrease the amounts retained by Prudential for contingency purposes. Amounts withdrawn are held in the SGLI revolving fund and are invested in U.S. Treasury Department securities. VA can use the SGLI revolving fund assets to stabilize and to augment participant premiums.

VA cash balances are maintained by the Treasury Department, and Life Insurance programs' receipts and disbursements are processed by the Federal Reserve System and Treasury. As required by Title 38, the Life Insurance programs invest in U.S. Treasury Securities.

The facilities occupied by the Life Insurance program offices in Philadelphia, St. Paul, and at VA Central Office are owned and maintained by the General Services Administration.

Policy Dividends

The Secretary of Veterans Affairs determines annually the excess funds available for dividend payment. Dividends payable are based on an actuarial analysis of the individual programs at the end of the preceding calendar year. Dividends are declared on a calendar year basis and paid on policy anniversary dates. Policyholders can elect: (1) cash payment, (2) prepay premiums, (3) repay loans, (4) purchase paid-up insurance, or (5) deposit in an interest-bearing account. A provision for dividends is charged to operations and an insurance dividend payable is established when gains to operations are realized in excess of those essential to maintain solvency of the insurance programs.

Insurance Program Liabilities

Most insurance liabilities are actuarially determined policy reserves representing the present value of future benefits less the present value of future premiums.

Liabilities for dividends payable in the subsequent fiscal year, dividends left on deposit and premiums paid in advance are included in Other Governmental Liabilities. The total Other Governmental liability of $1.9 billion is comprised of $0.3 billion for dividends payable, $1.4 billion for dividends left on deposit and $0.2 billion for premiums paid in advance.

Insurance Reserves

Insurance Reserve Balances as of September 30, 1998

Insurance Programs	Death Benefits	Death Benefit Annuities	Disability Income and Waiver of Premium	Other	Reserve Total
NSLI	$10,318	$213	$326	$70	$10,927
USGLI	57	9	0	0	67
VSLI	1,328	12	52	3	1,395
SDVI	410	1	95	1	508
VRI	449	2	12	1	464
VI&I	98	0	1	0	99
	$12,661	$238	$486	$75	$13,460
Less					
Unfunded Reserves					(524)
					$12,935

Note: SDVI and VI&I reserves include future policy benefits which are classified as Insurance Liabilities Not Covered by Budgetary Resources in the accompanying Balance Sheet.Actuarial reserve liabilities for VA life insurance programs are based on mortality and interest assumptions at time of issue. These assumptions vary by fund, type of policy and type of benefit. The interest assumptions range from 2.25% to 5.00%. The mortality assumptions include the American Experience Table, the 1941 CSO Table, the 1958 CSO Basic Table and 1980 CSO Basic Table.

Insurance In-Force

The amount of Insurance in-force is the total face amount of life insurance coverage provided by each VA insurance program as of the end of the fiscal year. It includes any paid-up additional coverage provided under these policies. The number of policies represents the number of active policies remaining in the program as of the end of the fiscal year.

VA Supervised and Administered Programs as of September 30, 1998

Supervised Programs:	**Number of Polices**	**Face Amount of Insurance**
SGLI Active Duty	1,457,000	$278,012
SGLI Ready Reservists	826,500	149,607
SGLI Post Separation	115,000	21,584
VGLI	367,950	31,471
Total Supervised Programs	2,766,450	$480,674
Administered Programs:		
National Service Life Insurance	1,906,825	$18,264
Veterans Special Life Insurance	240,394	2,730
Service-Disabled Veterans Insurance	156,745	1,452
Veterans Reopened Insurance	87,590	701
U.S. Government Life Insurance	19,660	65
Veterans Insurance and Indemnities	1,246	6
Veterans Mortgage Life Insurance	3,679	206
Total Administered Programs	2,416,139	$23,424
Grand Total - All Programs	5,182,589	$504,098

NOTE 15
Unexpended Appropriations

The total unexpended balance is the sum of undelivered orders and unobligated balances. Appropriation acts and other provisions of law provide authority to incur new obligations. An obligation represents an amount that is expected to be expended upon subsequent receipt of goods or services. The obligated balance is the cumulative amount of obligations incurred by VA for which outlays have not been made. Undelivered orders are the amount of goods and services ordered for which delivery or performance has not yet occurred and are included in this balance. An unobligated balance is the amount available after deducting the cumulative obligations from total budgetary resources. In some instances, unobligated balances are not available due to legal constraints regarding the time limit and purpose for which funds can be obligated.

Unexpended Appropriations as of September 30, 1998

	Unobligated		Undelivered	
	Available	Unavailable	Orders	Total
VHA	$1,734	$368	$2,092	$4,194
VBA	437	5	5	447
NCA	4	3	7	14
ADM	-	19	54	74
Total	$2,176	$394	$2,158	$4,729

NOTE 16 Contingencies

VA is a party in various administrative proceedings, legal actions, and tort claims brought by or against it, which ultimately results in settlements or decisions adverse to the Federal Government. These actions, claims, and cases arise from various sources including: disputes with contractors, challenges to compensation and education award decisions, loan guaranty indemnity debt cases, and allegations of medical malpractice.

Certain legal matters to which VA may be a named party are administered and, in some instances, litigated and paid by other Federal agencies. These primarily relate to allegations of medical malpractice, but also include other tort claims and contract disputes. Generally, amounts (more than $2,500 for Federal Tort Claims Act cases) to be paid under any decision, settlement, or award pertaining to these litigations are funded from a special appropriation called the Judgment Fund, which is maintained on deposit with the Department of the Treasury. Of the amounts paid from the Judgment Fund, malpractice cases claimed 82% in FY 1998. Contract dispute payments require reimbursement to the Judgment Fund by VA.

In accordance with OMB Interpretation No. 2 of Federal Financial Accounting Standards, VA has included a liability for pending legal claims that will probably be paid by the Judgment Fund. This liability is established for all pending claims whether reimbursement is required or not. This liability was $68.7 million for FY 1998. VA is also required to record an operating expense and imputed financing source for Judgment Fund pending claims and settlements. Judgment Fund accounting is shown below:

Judgment Fund

Fiscal Year settlement payments	$ 73.8
Less contract dispute payments	(7.5)
Imputed financing-paid by other entities	66.3
Increase (decrease) in liability for claims	45.9
Operating expense	$112.2

It is the opinion of VA's management and Office of General Counsel, that the ultimate resolution of legal actions still pending as of September 30, 1998, will not materially affect VA's operations or financial position especially when consideration is given to the availability of the Judgment Fund appropriation to pay some court settled legal cases.

Medicare carve-out claims for overpayment amounts collected by MCCR may have to be refunded. Various employer plans and their third party administrators have pending claims for overpayments to VA for Medicare-eligible insureds under "carve-out" policies. In November 1997

General Counsel issued an opinion which held Treasury appropriation 20X1807 as the proper account to charge for refunds of erroneous MCCR overpayments collected or recovered on or before June 30, 1997. Refunds of MCCR overpayments collected or recovered after June 30, 1997, will be charged to the Medical Care Collections Fund.

VA's Office of General Counsel does not believe that the carve-out claims pending with VA as of September 30, 1998 will materially affect VA's operations or financial position.

A current audit of medical care billings suggests some may have been overstated. It is not felt the overstatement would be material to the financial statements.

A recent judgment in a class action involving Vietnam veterans exposed to Agent Orange may result in an increase in retroactive claims that VBA will have to re-adjudicate and pay. The amount of any such increase is not known. VBA will not be in a position to make an estimate until they undertake and complete a manual review of the particular claims involved.

Obligations Related to Canceled Appropriations

The amount of unobligated and obligated authority relating to appropriations canceled on September 30, 1998 was $72 million. Any payments that may arise relating to canceled appropriations will be paid out of the current year appropriations in accordance with the provisions of the Expired Fund Control Act of 1990.

NOTE 17 Environmental Clean Up Costs

The Department of Veterans Affairs has recorded unfunded cleanup costs in the amount of $139.3 million for VHA and $.01 million for NCA for the year ending September 30, 1998. The majority of the unfunded liability involves asbestos removal, lead abatement, replacement of underground oil and gasoline tanks, decommissioning of waste incinerators, and costs associated with decontamination of equipment prior to disposal.

While some facilities have applied prevailing state regulations that are more stringent than federal guidelines, OSHA and EPA are the legal basis for regulations behind the majority of VA cleanup liabilities.

Estimated costs for these projects have been computed by the facility engineering staff based on similar projects already completed, or by independent contractors providing work estimates.

NOTE 18 Disclosures Related to the Statement of Budgetary Resources

- The net amount of budgetary resources obligated for undelivered orders at the end of the period:

  VA has obligations remaining at the end of each year for goods and services ordered but not yet received (undelivered orders). Aggregate undelivered orders amounted to $2.4 billion at September 30, 1998.

- Available borrowing authority and contract authority at the end of the period:

  VA does not have any contract authority. Housing credit had borrowing authority of $1.4 billion. VBA had borrowing authority of $3 million for making vocational rehabilitation direct loans

- Repayment requirements, financing sources for payment, and other terms of borrowing authority used:

  Housing credit borrowing was repaid to Treasury through the proceeds of portfolio loan collections, funding fees, and its sale of loans to Vinnie MAC trusts. The vocational rehabilitation loans generally had a duration of 1 year and repayment was made from offsetting collections.

- Adjustments during the reporting period to budgetary resources available at the beginning of the year (supplemental appropriation or recission):

MCCF received a shortfall appropriation of $20 million in September. Compensation, Pension, and Burial Benefits received a $550 million supplemental appropriation.

- Permanent Indefinite Appropriations:

VA has three permanent and indefinite appropriations. One is the Veterans Housing Benefit Program Fund (36x1119). It covers all estimated subsidy costs arising from post-1991 loan obligations for Veterans Housing Benefits. The fund's objective is to encourage and facilitate the extension of favorable credit terms by private lenders to veterans for the purchase, construction, or improvement of homes to be occupied by veterans and their families.

The Loan Guarantee Revolving Fund (36x4025) is a liquidating account which contains all of VA's pre-credit reform direct and guaranteed loans. It also holds fund balances received from reimbursements from Financing accounts for loan modifications and rentals of foreclosed properties not yet transferred to Financing accounts. This account is responsible for the property management expenses prior to sales of foreclosed property.

The Native American Direct Loan Account (36x1120) was established to cover all subsidy costs arising from direct loan obligations related to a veteran's purchase, construction, or renovation of a dwelling on trust land.

- Information about legal arrangements affecting the use of unobligated balances of budget authority, such as time limits, purpose, and obligation limitations:

Available unobligated balances on the final Statement of Budgetary Resources are composed of current fiscal year apportioned funds for annual, multiyear and no-year appropriations from Congress as well as revolving and trust funds. Other balances not available are composed of expired appropriation unobligated amounts which generally are not available for new obligations, but can be used to increase existing obligations under certain circumstances. This amount also includes unobligated funds that were not apportioned by OMB for FY 98 use.

Unobligated VA funds are available for uses defined in VA's FY 98 Appropriation Law (P.L. 105-065). These purposes include: veterans' medical care, research, education, construction and maintenance of VA buildings, veterans' and dependents' benefits, veterans' life insurance, housing credit programs, veterans' burial benefits and administrative functions.

Various obligation limitations are imposed on individual VA appropriations. Examples include travel obligation limitations and limitation of the use of medical care multi-year funds to object classes for equipment, structures and land.

- Explanations of any differences between information required by SFFAS No. 7 and the amounts described as "actual" in the Budget of the United States Government for that fiscal year:

To our knowledge, there are no differences.

- The amount of contributed capital received during the reporting period was as follows:

a) $42 million in donations were received by the General Post Fund.
b) $102 thousand in donations were received by the National Cemetery Gift Fund.

NOTE 19 Statement of Net Cost Disclosure

Cost of Stewardship PP&E

Costs related to the maintenance or renovation of heritage assets are expensed as incurred. Since the heritage assets of the VA are multi-use, that portion of costs directly associated with the preservation of the heritage class is recorded separately from general PP&E expensed or capitalized costs. Listed below is the heritage related cost reported for Heritage assets of the VA.

Heritage Assets Costs

	VHA	NCA
Buildings	$1.44	$.17

Exchange revenues - normally require reporting entities to recover full cost.

The Veterans Health Administration (VHA) has legislated exceptions to the requirement that user charges be sufficient to recover the full cost to the Federal Government of providing the service, resource, or good. Under "enhanced sharing authority" arrangements entered into shall provide for payment to the Department (VA) in accordance with procedures that provide appropriate flexibility to negotiate payment which is in the best interest of the Government.

VA's Loan Guaranty Line of Business collects rental fees on a small number of properties during the period when the property is titled to the VA.

The National Cemetery Administration leases lodges at 16 cemeteries to Not for Profit groups for no fee. The Not for Profit groups are required to provide the upkeep on the lodges and pay all other costs except for major repairs.

The National Cemetery Administration has leases with private companies/individuals for approximately 1,700 acres of undeveloped cemetery land, which is utilized for agricultural purposes. The lessee is required to pay all costs of maintaining the land.

Exchange transactions with the public - occur when prices are set by law or executive order and are not based on full cost or on market price.

The Department of Veterans Affairs Medical Care Collections Fund, "Conforming Amendments," changed the language of specific sections of 38 USC Chapter 17 to substitute "reasonable charges" for "reasonable cost." The VHA Chief Financial Officer (CFO) is responsible for implementing and maintaining these reasonable charges for billing third party payers for services provided to insured veterans for treatment of nonservice-connected conditions. Reasonable charges are based on provider charges in the market area of each VA facility. The lesser of VA billed charges or their usual customary and reasonable payment to other providers will be paid. Cost based per diems are

Schedule of Net Program Costs

	VHA			VBA						NCA	Total
	Medical Care	Medical Education	Medical Research	Compensation	Pension	Education	Vocational Rehabilitation	Loan Guaranty	Insurance	Burial	
Net Program Costs:											
Production Costs											
Governmental Costs	$2,041	$0	$607	$0	$0	$0	$0	$0	$0	$0	$2,648
Less: Earned Revenues	-93	0	-50	0	-15	-171	0	0	-1,165	0	-1,496
Net Governmental Production Costs	$1,948	$0	$557	$0	-$15	-$171	$0	$0	-$1,165	$0	$1,153
Public Costs	$15,887	$833	$20	$126,267	$3,243	$1,136	$502	$1,847	$2,141	$1,314	$153,190
Less: Earned Revenues	-798	0	-2	0	0	0	0	-469	-796	0	-2,065
Net Public Production Costs	$15,089	$833	$18	$126,267	$3,243	$1,136	$502	$1,378	$1,345	$1,314	$151,125
Non-Production Costs											
Hazardous Waste Clean-up	$139	$0	$0	$0	$0	$0	$0	$0	$0	$0	$139
NET PROGRAM COSTS	$17,176	$833	$575	$126,267	$3,228	$964	$502	$1,378	$180	$1,314	$152,417

calculated annually to produce Tort Rates used to bill for tort feasor, worker's compensation (other than Federal), humanitarian emergencies, ineligibles, VA employee, family member, allied beneficiary, no fault or uninsured motorist's insurance, or reimbursable insurance cases. These per diem costs are derived primarily from cost and workload data from a national cost allocation report (Cost Distribution Report).

The VA is required to collect a co-payment of $2 from veterans with a nonservice-connected condition for each 30-day supply of medication furnished on an outpatient basis. This fee does not cover the cost of the medications in the vast majority of cases.

VA's Loan Guaranty Line of Business collects certain fees that are set by law. The loan guaranty funding fees collected for the year was $602 million. The loan guaranty lender participation fees collected for the year were $1.5 million.

Intragovernmental exchange transactions -in which the entity provides goods or services at a price less than the full cost or does not charge a price at all with explanations for disparities between the billing and full cost.

The VA and the Department of Defense (DOD) have authority to enter into agreements and contracts for the mutual use or exchange of use of hospital and domiciliary facilities and other resources. The providing agency shall be reimbursed for the cost of the health-care resources based on the methodology agreed to by VA and DOD. Facility Directors have the flexibility to consider local conditions and needs and the actual costs of providing the services. VA's General Counsel has opined that full cost recovery is not mandated, VHA captures the total amount of reimbursements received under DOD sharing agreements.

When VA furnishes medical care or services for beneficiaries of other Federal agencies, and that care or service is not covered by an applicable local sharing agreement, then billing rates used are determined and published annually by the VHA CFO. Similar to the Tort Rates, interagency billing rates are determined from cost and workload data in the Cost Distribution Report.

The Benefits Line of Business collects funding from DOD in order to administer certain education programs within the line of business. DOD transferred $208 million during the year for the VEAP and the New GI Bill for Veterans. In addition, VBA collected $651 thousand from the Social Security Administration for work performed in Manila.

Specific goods or services made to order under a contract - require disclosure of the full amount of the expected loss when it is probable and measurable.

VA does not have any contracts where it makes specific goods or provides specific services.

FY 1998 Total Costs and Earned Revenue by Budget Functional Classification

700: Veteran Benefits & Services	VHA	VBA	NCA	ADM	TOTAL
Net Program Costs:					
Medical Care	$17,120	($4)	($6)	$66	$17,176
Medical Education	829	0	0	4	833
Medical Research	571	0	0	4	575
Compensation	19	125,997	(114)	365	126,267
Pension	4	3,069	0	155	3,228
Education	3	901	0	60	964
Vocational Rehabilitation and Counseling	3	421	0	78	502
Loan Guaranty	3	1,334	0	41	1,378
Insurance	1	174	0	5	180
Burial	20	1,198	90	6	1,314
Net Intra-VA eliminations/transfers	(18)	(131)	120	30	1
Total Net Program Costs:	$18,555	$132,959	$90	$814	$152,418
Costs Not Assigned to VA Programs	$0	$0	$0	$128	$128
Less: Other Earned Revenues not Attributable to VA Programs	$0	$0	$0	($102)	($102)
NET COST OF OPERATIONS	$18,555	$132,959	$90	$840	$152,444

NOTE 20 DEDICATED COLLECTIONS Disclosure

In the Federal Government dedicated collections are accounted for in trust funds and special funds. The term "Trust Funds" as used in this report and in Federal budget accounting, is frequently misunderstood. In the private sector, "trust" refers to funds of one party held by a second party (the trustee) in a fiduciary capacity. In the Federal budget, the term "trust fund" means only that the law requires the funds be accounted for separately and used only for specified purposes and that the account was designated as a "trust fund." A change in law may change the future receipts and the terms under which the fund's resources are spent. The "trust fund assets" represent all sources of receipts and amounts due the trust fund regardless of source. This includes "related governmental trans-

Funds within VA Receiving Dedicated Collections

Fund Name	Fund Type	Treasury Symbol	Authority to Use	Purpose of Fund	Financing Sources Public or Federal
Medical Care Collections Fund	Special	36x5287	Public Law 105-33	Accumulates recoveries from third parties and patient co-payments.	Public, primarily insurance carriers.
Escrowed Funds for Shared Medical Equipment Purchases	Deposit	36x6019	106 Statute 1974	Receives payments from public companies involved in joint purchases of medical equipment.	Public universities pharmaceuticals and other medical organizations.
Personal Funds of Patients	Deposit	36x6020	38 USC §3204	Temporarily holds funds.	Public, patients.
Employee Allotments for Savings Bonds	Deposit	36x6050		Temporarily holds funds.	Employees.
Cemetery Gift Fund	Trust	36x8129	38 USC §1007	Expenditure of funds is limited to cemeteries by donor	Public donors.
National Service Life Insurance Fund	Trust	36x8132	38 USC §720	Accumulates premiums to insure veterans of WW II.	Public, veterans.
Post-Vietnam Era Education Assistance Program	Trust	36x8133	38 USC §1622	To subsidize the cost of education to veterans.	Both, VA and DoD contribute.
U.S. Gov. Life Insurance	Trust	36x8150	38 USC §755	Premiums insure WWI veterans.	Public, veterans.
Veterans Special Life Insurance Fund	Trust	36x8455	38 USC §723 Public Law 101-228	Premiums insure Korean War Vets without Service-related disabilities.	Public, veterans.
General Post Fund, National Homes	Trust	36x8180	38 USC Public Law 101-228	Receives restricted and unrestricted use donations	Public, mostly veterans.

Note: The table summarizes the name, type and purpose of the funds within VA that receive dedicated collections. Special funds pertaining to the Housing Credit program loan guaranty and direct loan activities are not included in the table because they only receive transfers for upward re-estimates of subsidy expense. These funds are shown as non-entity assets on the balance sheet. There are some special funds that are similar in nature to trust funds. For this discussion, the term trust funds includes those special funds that are similar in character to trust funds.

actions," which are transactions between two different entities within the Federal Government. The "Investments with Treasury" assets are comprised of investments in Federal debt securities, and related accrued interest. These securities will require redemption if a fund's disbursements exceed its receipts. Unless specifically provided for by law, trust funds may only place excess funds in a Federally backed investment (e.g. Federal debt securities).

Accounting and Reporting

All of the funds listed above use the accrual basis of accounting. However, collections are reported as actually received in accordance with OMB Circular A-34. The insurance funds listed above also adhere to the requirements of FASB No. 120 "Accounting and Reporting by Mutual Life Insurance Enterprises" and issue a separate annual report. All of the above funds generally receive authority to use all current year contributions as well as a portion of previously contributed amounts.

Condensed Information on Assets, Liabilities and Fund Balance

Fund Symbol	5287	6019	6020	6050	8126	8128	8129	8132	8133	8150	8455	8180
Assets												
Fund balance with Treasur	$ 53	-	$50	$ 2	$-	$-	$ -	$ 10	$123	$ -	$ 2	$ 3
Investments with Treasury	-	1	-	-	-	-	-	12,245	-	87	1,664	46
Other Assets	380		-	-	-	-	3	760	2	5	113	29
Total Assets	$ 433	$ 1	$50	$ 2	$-	$-	$ 3	$13,015	$125	$ 92	$1,779	$ 78
Liabilities												
Payables to Beneficiaries	$ -	$ -	$50	$ 2		$-	$ -	$ 1,654	$ 3	$ 21	$ 294	$ 2
Other Liabilities	-	1	-	-	-	-	-	10,928	-	67	1,395	-
Total Liabilities		$ 1	$50	$ 2	$-	$-	-	$12,582	$ 3	$ 88	$1,689	$ 2
Net Position												
Cumulative Results	433	-	-	-	-	0	3	433	122	4	90	76
Total Liabilities & Net Posi	$ 433	$ 1	$50	$ 2	$-	$-	$ 3	$13,015	$125	$ 92	$1,779	$ 78

Condensed Information on Net Costs and Changes in Fund Balance

Fund Symbol	**5287**	**8129**	**8132**	**8133**	**8150**	**8455**	**8180**
Revenues							
Exchange - Federal	$ 8	$ -	$ 970	$ -	$ 6	$145	$ -
Exchange - Public	570		658			78	
Non-Exchange -Federal							
Non-Exchange -Public							45
Total Revenues	**$578**		**$1,628**	$ -	**$6**	**224**	**45**
Expenses							
Program Expenses	$98		$1,573	$9	$11	$200	$40
Other Expenses			107		(5)	34	
Total Expenses	**$98**		**$1,680**	**$9**	**$6**	**$234**	**$40**
Net Change from Operations							
Beginning Net Position	$794	$3	$134	$147	$2	$43	$70
Net Change from Operations	480		(52)	(9)		(10)	5
Non-Operating Changes	(840)		351	(17)	2	57	
Ending Equity	$433	$ 3	$ 433	$122	$ 4	$ 90	$75

NOTE 21 Statement of Financing Note Disclosure

The total amount of VA liabilities not covered by budgetary resources was $581.4 billion as of September 30, 1998. The following table contains the components of the balance sheet liability:

Workers Compensation*	$ 1,621
Annual Leave	$882
Judgment Fund	67
Environmental & Disposal	139
Capital Leases	3
Veterans Compensation	578,149
Insurance	524
Total	$581,385

*The actuarial estimate for workers compensation provided by DOL was computed using an interest rate of 5.6%

The Statement of Financing line "total financing sources yet to be provided" only reflects the amount of increases in these liabilities. For existing liabilities there will always be a difference between the "financing sources" line and the balance sheet amount.

Note 22 Prior Period Adjustments and Changes in Accounting Principles

The following table summarizes prior period adjustments that were made to the beginning balances of certain funds as a result of changes in accounting principles or correction of errors.

Total Net Position Reported as of 9/30/97	$ (453,659)
Prior Period Adjustments:	
VBA Insurance programs' adoption of AICPA Statement of Position No. 95-01 which had the affect of reducing the liability for insurance reserves.	425
VHA redetermined the amount previously recorded as an extraordinary loss. The redetermination had the affect of increasing the loss recognized in the prior period and thereby decreasing beginning net position.	(9)
The Franchise fund within the Departmental Administration reporting segment understated total expenses for the prior period, thereby decreasing beginning net position.	(3)
Within the VBA reporting segment, there was a revaluation of the non-federal accounts receivable as of 9/30/97 which had the affect of increasing total assets and beginning net position.	2
The Supply fund within the Departmental Administration reporting segment identified amounts that were recorded as accounts payable but should not have been. This reduced total liabilities and increased beginning net position.	1
Total prior period adjustments	416
Total Beginning Net Position after Adjustments	$ (453,243)

In addition, there was a change in VA's reporting practices pertaining to special receipt accounts for subsidy re-estimates. VBA Housing credit programs' adoption of OMB guidance for negative subsidy re-estimates had the affect of increasing the Non-entity Assets and the related "Other Intragovernmental liabilities" as of 9/30/97 by $947 million. Total net position was not affected.